

NEWS BRIEFS

FTC PROPOSES NEW RULES FOR ENDORSEMENTS, TESTIMONIALS

The Federal Trade Commission (“FTC”) has issued proposed changes to its advertising guides (“Guides”) regarding the use of endorsements and testimonials. The Federal Register notice about the proposed

Guides can be found at (<http://www.ftc.gov/os/fedreg/2008/november/081128guidesconcerningtheuseofendorsementsandtestimonials.pdf>). The deadline for commenting on the proposed Guides is March 2.

Several years in the making, the Guides would change how the FTC

considers a firm’s obligations to accurately use testimonials to promote its products and services. Under current guidelines, the FTC allows a marketer to use a disclaimer such as “results are not typical” to avoid misleading consumers, with some restrictions. But FTC-commissioned research, cited in the *Federal Register* notice, indicates that many

continued on page 8

Court Watch

continued from page 6

weighing the deconstructed sandwich after cooking, etc.) and inconsistent and arbitrary application to franchisees (effectively punishing Defendants for choosing to call rather than e-mail in response to the termination notice, when the letter itself makes no distinction between the two methods of contact). Although the franchise agreement gave Quiznos the right to terminate the agreement if Defendants engaged “in conduct that, in the sole judgment of [Quiznos], materially impairs the goodwill associated with [Quiznos’ trademarks and service marks],” the court found that Quiznos had a duty under Colorado law to exercise that judgment reasonably, and held that Quiznos’ claim that the failure of a single sandwich to meet Quiznos’ standards was not a reasonable basis to find a material impairment of goodwill.

Moreover, the court found that by permitting Defendants to continue operating their store after sending the termination notice, Quiznos had waived its right to terminate the Defendants’ agreement, and was also estopped from asserting that right due to Defendants’ reliance on that permission.

Interestingly, instead of granting Defendants typical contract damages for Quiznos’ breach, the court found that rescission-type damages that attempted to put the parties into their respective positions from before entering into the agreement were more appropriate, due to the brief time between when Defendants assumed the agreement and when Quiznos attempted to terminate the agreement, and due to the

unusual nature of the “shadow” period during which Defendants operated the store but with little or no support from Quiznos. Ultimately, by attempting to use the field test “charade” to justify the purported termination of Defendants franchise agreement, the court found that Quiznos had itself violated the agreement and exposed itself to liability to its franchisee.

COMPETING RESTAURANTS EACH INCUR PARTIAL LOSS OF TRADEMARK RIGHTS

In September 2008, the U.S. District Court for the Eastern District of New York found that two competing restaurants with similar names should be ordered to use names sufficiently different to allow consumers to distinguish between the two. The court also found that, because one of the restaurants had failed to adequately enforce the terms of the license agreements by which it had licensed third parties to use its marks, that restaurant had abandoned those licensing marks, which in the case of such “naked” licensing, results in the trademark owner forfeiting the abandoned portion of the uncontrolled marks. *Patsy’s Italian Restaurant, Inc. v. Banas d/b/a Patsy’s*, 575 F. Supp. 2d 427 (E.D.N.Y. 2008).

Plaintiff Patsy’s Italian Restaurant (“Plaintiff”) brought actions against Defendant Patsy’s Pizzeria (“Defendant”) for federal service mark and trademark infringement, and for trademark infringement and unfair competition under New York law. For over 60 years, the parties had been sharing the mark Patsy’s for nearly identical restaurant-related services within the New York City market, with Plaintiff having registered a

mark including the Patsy’s name for restaurant services, and Defendant later having registered a similar mark, but in connection with its operation of a pizzeria. The parties had been vigorously litigating this and related lawsuits for many years, and this decision followed a jury trial.

The court’s opinion primarily focused on complicated issues of trademark law, in which matters are interesting in their own right and certainly relevant to franchisors and franchisees, but the decision also contained an interesting discussion regarding a trademark licensors’ obligation to enforce the terms of its licenses so as to ensure that its licensees do not exceed the authorized scope of use of the license marks. On this issue, the court found that, by allowing two licensed restaurants to provide services beyond those for which it claimed trademark protection, Defendant had failed to exercise sufficient quality control over those two franchised locations, and therefore the law supported Defendant losing a portion of its rights in the licensed marks, as opposed to losing all such rights, as would be the case in other types of trademark abandonment.

Also of note is the truly unusual nature of the relief granted by the court, which invalidated federally registered trademarks held by both Plaintiff and Defendant, enjoined both parties from using the mark Patsy’s alone, and ordered Plaintiff to refer to its restaurant services using the mark Patsy’s Italian Restaurant, and Defendant to refer to its pizzeria services using the mark Patsy’s Pizzeria.



MOVERS & SHAKERS

MARKUS COHEN: 1940-2009

Markus Cohen, Q.C., a franchise attorney in Toronto, Canada, and a member of *FBLA's* Editorial Board, passed away Jan. 11, 2009. Cohen was the founder of The Virtual Law Firm®. Among his many contributions to the profession, Cohen was a member of the Legal and Legislative Affairs Committees of both the Canadian Franchise Association and the International Franchise Association.

Attorney **Frank Zaid** (Osler, Hoskin & Harcourt LLP, Toronto) described Cohen as “a true gentleman, a wise

counsel, a polished professional, an aristocrat, and a person who enjoyed life to the fullest.”

Cohen is survived by his wife, **Nita**, three children, and four grandchildren. Donations may be made to the Princess Margaret Hospital Foundation in Toronto for its Lung Screening Program.

FRANCHISING COMMITTEE NAMES NEW EXECUTIVE BOARD

The new board of the International Bar Association's Franchising Committee took office Jan. 1, 2009.

The new board is: **Andy Scott**, past chair (Paul, Hastings, Atlanta); **Penny Ward**, chair (Baker McKenzie, Sydney, Australia); **Jorge Mondragon**, senior vice chair (Gonzalez Calvillo, Mexico City); **John Baer**, vice chair (Sonnenschein Nath, Chicago); **Rocio Belda**, secretary/Web site officer (Garrigues, Madrid); **Marco Hero**, publications officer (Tigges, Dusseldorf, Germany); **Andrew Loewinger**, newsletter editor (Nixon, Peabody, Washington, D.C.); and **Lou Jones**, corporate counsel liaison (Papa John's, Louisville, KY).



News Briefs

continued from page 7

customers believe they and other purchasers will get the same results as the endorser recites, even if those results are not representative of a typical experience. The FTC's proposed solution is that marketers provide “an affirmative disclosure of the results that are typical.”

What is “typical”? The FTC proposed to define that, too. The advertiser must have “evidence that the endorser's experience is representative of what consumers will generally achieve with the advertised product in actual, albeit variable, conditions of use,” wrote the FTC. As a general rule, the FTC suggested that “representative” reflects the outcome for half of the users of the product or service.

The proposed new Guides also give examples for the first time of how the rules would apply to marketing claims over which the company does not have direct control, such as word-of-mouth information passed along from one consumer to another. Reflecting the development of online promotions, the Guides would incorporate the “potential liability of advertisers who use bloggers to promote their products and of the bloggers themselves,” if those bloggers make misrepresentations.

Although the Guides are advisory in nature (not a trade regulation rule with the force of law, like the Franchise Rule), the proposed changes could have a significant impact on franchisors and franchisees who use customer testimonials in advertising products and services, or who use franchisee testimonials in marketing franchise opportunities. “The difference between Guides and a trade regulation rule, such as the Franchise Rule, is simple,” said **David Koch, Plave Koch PLC (Reston, VA)**. “If you do something contrary to the Franchise Rule, you have violated the law. If you do something contrary to the Guides, you might (or even probably) have violated the law, but the FTC still has to prove that the particular endorsement or testimonial was deceptive as used.”

Koch provided the following example. Franchisors often use customer endorsements to promote the goods and services of the brand, and some franchisors use endorsements from existing franchisees to promote the franchise opportunity. “The impact from the proposed changes in the Guides will depend on how detailed the endorsement is,” he said. “The main question is whether the endorsement conveys specific results that are not likely to be typical for other purchasers. A generic endorsement like ‘this is a great product,

or ‘I've had a good experience with this franchise’ is not going to be affected. On the other hand, a specific endorsement like, ‘I lost 30 pounds’ or ‘I've doubled my income with this franchise’ will be greatly affected if the franchisor knows that the stated results are not typical. If the proposed changes are adopted, which seems pretty likely, the franchisor will have to add a statement disclosing the results that are typical. So in the first example, the franchisor would have to add, ‘The typical customer loses 5 pounds.’”

While much of the discussion in the Guides reflects problems with weight-loss claims, the application of the rules is much broader. “Obviously, the affirmative disclosure of typical results will dilute the impact of the individual endorser's results — which is exactly what's intended by the FTC,” said **Koch**. “In practice, the requirement may discourage franchisors and other advertisers from using any endorsements that convey specific results.”



The publisher of this newsletter is not engaged in rendering legal, accounting, financial, investment advisory or other professional services, and this publication is not meant to constitute legal, accounting, financial, investment advisory or other professional advice. If legal, financial, investment advisory or other professional assistance is required, the services of a competent professional person should be sought.

To order this newsletter, call:
1-877-256-2422

On the Web at:
www.ljnonline.com